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STATEMENT OF VINCE MALTA ON BEHALF OF THE NATIONAL ASSOCIATION OF REALTORS®

Before the

The Senate Committee on Banking, Housing and Urban Affairs

"AN EXAMINATION OF THE NATIONAL FLOOD INSURANCE PROGRAM"

October 2, 2007

Introduction

Thank you, Chairman Dodd for inviting me to testify today before the Committee on Banking, Housing and Urban Affairs and present the views of the National Association of REALTORS® (NAR) on the National Flood Insurance Program.

My name is Vince Malta. I am the owner and broker of Malta & Co., Inc, a San Francisco California firm handling real property sales and management of over 300 residential rental units. I am a member of the California Association of REALTORS® and National Association of REALTORS® and have held a number of leadership positions in both associations, including serving as the 2006 President of the California Association of REALTORS® and the 2007 Vice-Chair of the Public Policy Coordinating Committee for the National Association of REALTORS®.

The National Association of REALTORS® is America's largest trade association, representing more than 1.3 million members involved in all aspects of the residential and commercial real estate industries. NAR is the leading advocate for homeownership, affordable housing and private property rights.

Overview

The National Flood Insurance Program (NFIP) has been effective in reducing the costs of flood damage both to property owners and the government. A recent study of the NFIP, found that the program "has clearly induced savings on flood costs" and that "flood insurance has shifted the loss from taxpayers to those who pay the insurance premium."[1] According to FEMA,

[1] Pacific Institute for Research, "Costs and Consequences of Flooding and the Impact of the National Flood Insurance Program," (prepared as part of the 2001-2006 Evaluation of the National Flood Insurance Program), (Calverton, MD: October 2006), p. 28 (hereafter, "PIR Study").

flood damage is reduced by nearly $1 billion a year as the result of communities implementing sound floodplain management requirements and property owners purchasing flood insurance.[2]

Although the NFIP has been effective at reducing costs to property owners and the federal government, flood damage during 2004 and 2005 has shown the need for reforming the program to better protect more people at risk and to put the program on a stronger financial footing.

Legislation to reform the NFIP should: 1) ensure that flood maps are accurate and up to date; 2) address the NFIP's ability to pay existing and future obligations to policyholders; and 3) educate consumers about the importance of obtaining and maintaining flood insurance, which could in turn lead to increased participation in the NFIP. Though supportive of reforms to the NFIP, REALTORS® are concerned that some proposals could have undesired impacts on certain segments of the population, neighborhoods and communities. NAR encourages Congress to strike a balance between ensuring the long-term fiscal viability of the NFIP and avoiding changes that may result in market inequities and housing affordability problems, especially for low- and moderate-income homeowners and renters.

The National Association of REALTORS® encourages the committee, as it develops legislation to reform the NFIP to consider the findings of a report released in October 2006 that found "[t]he common belief that the NFIP has stimulated development that increased flood losses is not supported by our findings."[3]

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[2] See: http://www.fema.gov/about/programs/nfip/index.shtm.

[3] PIR Study, p. 41. The study also notes that the subsidy may prevent some properties, especially those located below base flood elevation (BFE), from being replaced or substantially renovated, which would lead to a removal of the subsidy on these properties. As noted below on pages 7-8, NAR supports adding demolition and rebuilding as a mitigation measure, which would have the effect of removing the subsidy on these properties.

The Importance of the National Flood Insurance Program

A strong real estate market is the linchpin of a healthy economy, generating jobs, wages, tax revenues and a demand for goods and services. In order to maintain a strong economy, the vitality of residential and commercial real estate markets must be safeguarded.

The National Flood Insurance Program is a unique partnership among property owners, all levels of government, and the private sector. It enables property owners in participating communities to purchase insurance as a protection against flood losses in exchange for state and community floodplain management regulations that reduce future flood damages. More than 20,000 communities throughout the United States and its territories participate in the NFIP and have adopted floodplain management ordinances. In each of these communities, the NFIP makes federally-backed flood insurance available to homeowners, renters, and business owners. As a result of these proactive efforts, federal expenditures for disaster assistance and flood control are reduced.

Since its creation, the National Flood Insurance Program has helped to mitigate the escalating costs of repairing damage to buildings and their contents caused by floods. Buildings constructed in compliance with NFIP building standards suffer approximately 80 percent less damage annually than those not built in compliance. According to FEMA, flood damage is reduced by nearly $1 billion a year as the result of communities implementing sound floodplain management requirements and property owners purchasing flood insurance.

As of August 2006, the NFIP has paid more than $17.3 billion in claims for the 2005 floods.[4] This amount is greater than all claims paid out by the NFIP up to that point in time. In prior years, when losses exceeded the NFIP's ability to pay claims, the program was able to

[4] Government Accountability Office, "High-Risk Series: An Update," (January 2007), p. 91.

borrow money from the U.S. Treasury and pay it back with interest. The very sizeable flood losses resulting from the 2005 storm season have made people take a closer look at the NFIP.

Understandably, many members of Congress, after voting to increase the NFIP's borrowing authority three times, are seeking to reform the NFIP. The National Association of REALTORS® agrees that, given the importance of the NFIP to communities across the country, it is critical that the program be financially stable. Congress, FEMA, and industry stakeholders, working together, can make a number of changes to ensure that the NFIP rests on a solid footing well into the future.

Three Essential Elements of NFIP Reform Legislation

The National Association of REALTORS® encourages efforts to reform the NFIP that will: 1) ensure that flood maps are accurate and up to date; 2) address the NFIP's ability to pay existing and future obligations to policyholders; and 3) educate consumers about the importance of obtaining and maintaining flood insurance, which could in turn lead to increased participation in the NFIP. In addition, reform efforts should strike a balance between ensuring the long-term fiscal viability of the NFIP and avoiding changes that may result in market inequities and housing affordability problems, especially for low- and moderate-income homeowners and renters.

1. Accurate Flood Maps

As a necessary first step to providing flood insurance and implementing floodplain management regulations, the NFIP identifies and maps the nation's floodplains. This mapping process provides the data needed to design effective floodplain management programs, actuarially rate flood insurance policies, and create public awareness of which areas are subject to flood hazards. Accurate and up-to-date flood maps are the keystone to the NFIP.

The National Association of REALTORS® strongly supports FEMA's map modernization efforts. Without accurate maps, property owners are not able to properly evaluate the risk to their property from flooding. NAR has been, and will continue to be, a strong advocate of fully funding the map modernization program.

FEMA has been engaged in a map modernization program to update and digitize the flood maps for the 100-year floodplain for several years. According to a report by the General Accounting Office submitted to the Chair of the House Subcommittee on Housing and Community Opportunity in March 2004, when Congress appropriated funds in FY 2003 to allow FEMA to undertake a full-scale update of the nation's flood maps, FEMA expected the effort to take five years to complete. [5]

NAR is concerned, however, that a requirement to map the 500-year floodplain – a task much larger than updating the existing 100-year floodplain maps – as part of FEMA's map modernization program could lead to delays in updating the 100-year floodplain maps, now scheduled to be completed in 2010. REALTORS® do not want to see this process delayed further. NAR believes that the ongoing efforts to update the 100-year floodplain maps should be completed before any effort to map the 500-year floodplain is undertaken.

On a separate, yet related issue, NAR supports reestablishing the Technical Mapping Advisory Council (TMAC) and strongly encourages the Committee to add a real estate professional to the TMAC membership. A real estate professional will be able to provide the perspectives of map users, including homeowners and potential homebuyers, and provide a user's perspective regarding how these maps impact real estate transactions.

2. Promoting Financial Stability

Reforms to the NFIP certainly will need to address the outstanding debt, increase revenues to the NFIP and decrease outlays. As a result of 2004 and 2005 flood damage, the NFIP owed the U.S. Treasury $17.5 billion as of May 2007.[6] As the Congressional Budget Office (CBO) has acknowledged, the NFIP "does not generate regular surpluses of the size needed to cover catastrophic losses."[7] CBO does acknowledge, however, that the NFIP "operated as a largely self-financed program for many years, occasionally borrowing relatively small amounts from the Treasury and repaying them."[8] There are a number of policy options to address NFIP financial stability that would have the support of REALTORS® and others where we would urge Congress to consider carefully.

Repetitive Loss Properties The National Association of REALTORS® supports policies and reforms that would limit the drain on the NFIP posed by severe repetitive loss properties. These properties, though a small percentage of properties covered by the NFIP, receive a disproportionate share of payouts from the program. NAR supports "full risk" premiums for flood insurance on repetitive loss structures that have repeatedly (i.e., more than two occurrences) suffered insured flood losses and have declined a reasonable offer of mitigation funding from FEMA, except in states which have been granted a federal exemption.

Repetitive loss properties pose a significant financial burden to the NFIP. Research conducted by the Multihazard Mitigation Council of the National Institute of Building Sciences

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[5] U.S. General Accounting Office, "Flood Map Modernization: Program Strategy Shows Promise, but Challenges Remain," GAO 04-417, March 2004, p. 8.

[6] General Accountability Office, "National Flood Insurance Program: FEMA's Management and Oversight of Payments for Insurance Company Services Should be Improved," GAO-07-1078, (Washington, D.C.: September 5, 2007), p. 10.

[7] Congressional Budget Office, "Value of Properties in the National Flood Insurance Program," (Washington, D.C.: June 2007), p. 1 (hereafter "CBO Report").

[8] Ibid.

found that a dollar spent on mitigation saves society an average of four dollars.[9] NAR supports amending the flood mitigation assistance program to allow "demolition and rebuilding" as a mitigation measure. In addition, NAR supports funding for mitigation activities for individual repetitive loss properties, and extending the pilot program for mitigation of severe repetitive loss properties.

Increased Participation Understandably, there is a desire to increase the money paid into the NFIP as a means of ensuring the financial solvency of the program. One way to help support the future stability of the NFIP is to increase participation in the NFIP by those properties most at risk of suffering flood damage. A 2005 study by the RAND Corporation showed that, in Special Flood Hazard Areas (SFHAs), those areas deemed by FEMA most likely to suffer flood losses and where flood insurance is mandatory for property owners with federally-backed mortgages, only about 50% of properties have flood insurance.[10] Increasing market penetration would lead to increased funds for the NFIP, would help protect property owners recover from flood losses, and could help decrease future federal assistance when uninsured properties flood and suffer loss.

According to a recent report on the NFIP, "knowledge of low-income issues is spotty."[11] Moreover, flooding from recent hurricanes in the Gulf Coast as well as in North Carolina has raised concerns that vulnerable low-income families have virtually no coverage.[12] Therefore, the National Association of REALTORS® encourages the committee to include a study in its NFIP reform bill that would identify ways to increase low-income family participation in the NFIP and identify ways to ensure that a greater percentage of at-risk homeowners and renters are able to

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[9] Multihazard Mitigation Council, "Natural Hazard Mitigation Saves: An Independent Study to Assess the Future Savings from Mitigation Activities, Volume 1 – Findings, Conclusions and Recommendations," National Institute of Building Sciences, Washington, D.C. (2005), p.5.
[10] See PIR Study, p. 36.
[11] PIR Study, p. 43.
[12] Ibid.

protect themselves from future flood losses. We believe that any such study should include an analysis of how best to encourage renters to participate in the NFIP because they too are at risk and eligible to purchase content insurance.

Increased Coverage Limits Offering additional coverage to those already participating in the NFIP should also be encouraged. Increasing maximum coverage limits for residential properties, non-residential properties, and contents coverage would more accurately reflect increases in property and contents values and provide fuller coverage to policyholders. In addition, providing additional coverage for living expenses, basement improvements, business interruption and replacement cost of contents would help protect homeowners and business owners.

Mandatory Purchase Requirements Another option to increase revenues to the NFIP is to expand the mandatory purchase requirement to properties located behind levees and dams and in the 500-year floodplain. The National Association of REALTORS® encourages the committee to proceed cautiously when considering expanding the scope of the mandatory purchase requirement. NAR encourages the committee to include in its NFIP reform legislation a study to examine the effects of such an expansion on homeowners and renters.

Debt Coverage The outstanding debt owed to the Treasury by the NFIP also must be addressed. According to the CBO, the NFIP debt can be expected to grow by $900 million per year, given the current mix of policies.[13] In the 109th Congress, legislation passed by this committee would have forgiven the debt and created a long-term reserving mechanism to address future catastrophic losses on the scale experienced in 2005 and 2005. NAR encourages the committee to consider such an approach again in its NFIP reform bill.

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[13] CBO Report, p. 1.

Subsidy Elimination Eliminating subsidies in the NFIP is another idea that has been considered. The National Association of REALTORS® strongly encourages this committee to commission a study of the effects of phasing out subsidies on primary residences, non-primary residences and non-residential properties before including such a proposal in legislation. Properties built under the same circumstances and facing identical flooding risks should not be charged different premiums. While proponents of eliminating subsidies on non-primary residences and non-residential properties argue that such a change would make the NFIP more fiscally sound, there may be significant unintended consequences for renters, business owners, potential homebuyers, neighborhoods and local economies.

According to a CBO report on the NFIP released in June, "**the evidence here does not suggest that the subsidies tend to cover larger or more luxurious structures, whether inland or in a coastal area**."[14] [emphasis added] The same report also notes that coastal subsidized properties tend to be more valuable than coastal unsubsidized properties, but that the reverse is true for inland properties where unsubsidized properties are more valuable than subsidized properties.[15] Another study on the NFIP found that those in the middle-income brackets were less prone to live in higher flood hazard areas than either those in the highest or the lowest income brackets.[16] That study noted that "low income households [defined as $10,000 - $30,000/year] live in hazardous areas in order to find affordable housing or because they work in water recreation areas and find the least expensive housing nearby."[17]

The National Association of REALTORS® is concerned that eliminating subsidies would result in higher flood premiums, increase the cost of property ownership and rents in these areas, and could lead to increasing delinquencies, foreclosures and reduced property values. FEMA

[14] CBO Report, p. 7.
[15] CBO Report, p. 8.
[16] PIR Report, p. 43.

estimates that if the average subsidized policy were to pay its full-risk premium, that premium would be increased to $1,800 per year, or about two and a half times the current level; some properties could see premiums increase four-fold or more. There is a limit to the amount that insurance, or any other operating expense, can increase before owners are either forced to raise rents, sell their properties, or go without insurance. In the case of residential rental properties, it is especially likely that a significant portion of single-family property owners would be hard pressed to absorb such a cost increase without raising rents.

3. Educating Consumers

Educating consumers is essential to help protect against future loss from flooding. Many consumers may not be aware that flood insurance is available to them, especially if they live outside a high-risk flood area. The National Association of REALTORS® strongly encourages the committee to include education and information policies in its NFIP reform bill. As noted above, only about 50% of homeowners in high-risk flood areas purchase flood insurance. Unfortunately, floodwaters do not know or care which properties are insured.

REALTORS® play a role in educating consumers by increasing awareness of the NFIP and providing information on obtaining coverage. In addition, NAR has been working with FEMA to develop educational materials for REALTORS®, clients, and potential clients about the importance and availability of flood insurance through the National Flood Insurance Program. These materials should be finalized later this fall.

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[17] Ibid.

Conclusion

Thank you again for inviting me to present the views of the National Association of REALTORS® on the National Flood Insurance Program. The National Association of REALTORS® stands ready to work with the members of the Committee on Banking, Housing and Urban Affairs to develop meaningful reforms to the National Flood Insurance Program that will help protect homeowners, prospective homeowners, renters, and commercial property owners prepare for and recover from future losses resulting from floods.